UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK
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BLACKROCK ALLOCATION TARGET SHARES: SERIES S PORTFOLIO, et al.,

Plaintiffs,

v. 14 CV 9401 (PGG)

U.S. BANK NATIONAL ASSOCIATION,

Defendant.

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New York, N.Y.
January 31, 2018
9:40 a.m.

Before:

HON. PAUL G. GARDEPHE,

District Judge

APPEARANCES

BERNSTEIN, LITOWITZ, BERGER & GROSSMAN
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(In open court, case called)

THE COURT: All right. This case was reassigned to me from Judge Forrest. It's on my calendar today for purposes of a hearing on plaintiff's motion for class certification. I'm prepared to rule on the motion. However, I'm happy to hear anything the lawyers want to say before I do so.

Mr. DeLange, is there anything else you want to add to the papers at this point?

MR. DeLANGE: Your Honor, if I could be brief, I would like to add a few points I would like to highlight to our papers.

THE COURT: Go ahead.

MR. DeLANGE: The main point I want to highlight is this is a straightforward motion for class certification under Second Circuit authority and authority in this district. Focusing on the common questions, you focus on liability, and how are we going to prove liability in this case. This case is brought by hundreds of class members involving claims against U.S. Bank for breach of contract, breach of the Trust Indenture Act.

Those questions on U.S. Bank's liability are common to all members of the class. The answers to those questions will be proven through common evidence. And specifically, it will be proven through standardized contracts that set forth the exact same responsibilities that U.S. Bank has to every single

member of the class. There is not a different contract for individualized members of the class. It is the exact same contracts, the exact same duties, the exact same obligations. It is common to every single member of the class.

In addition, you will have common evidence that will show U.S. Bank's -- starting with the existence of breaching loans within these trusts, common evidence from remittance reports, from the performance of those loans, from the loan files, all of that evidence will be used by every single member of the class to show that there were breaches of representations and warranties.

In addition, class members will utilize common evidence to show U.S. Bank discovered the breaches of representations and warranties. That common evidence will be information from U.S. Bank's files, it will be testimony from their personnel. That's how every single class member will show that U.S. Bank discovered breaches of reps and warranties. There are no individualized questions with respect to U.S. Bank's liability. The same holds true for the servicing violations. Every class member will answer the common question with common evidence showing the common answers. That's the focus on class certification.

We meet each of the elements of Rule 23(a), and we also meet the elements of 23(b)(3), which is predominance and superiority. I want to to focus quickly on predominance, which

again focuses on commonality, which I addressed, but it's a deeper dive, and the Court has to look further into whether or not the common questions predominate over any individualized ones.

In their papers, U.S. Bank raises certain speculative defenses to the claims, but the key is U.S. Bank raises no individualized questions with respect to core issue the fundamental issue in this case, which is U.S. Bank's liability for breach of contract as the trustee over these indentured trusts. Those questions will all be answered with common evidence, and those questions predominate over any individualized questions.

I want to quickly address a few of their arguments, and then I will open it up if the Court has any questions.

First, U.S. Bank argues that New York law doesn't apply to the transfer of these securities, and that the Court is going to have to engage in individualized inquiry and discovery into each individual transfer of the securities, essentially tracing the purchase of these securities all the way back to the initial offering. That's untrue.

General Obligations Law 13-107 applies to this case. It is exactly on point with Judge Koeltl's decision in *Excelsior*. The notes at issue in this case expressly state that New York law governs. That was issue before Judge Koeltl in the *Excelsior* case, and he found that New York law applied,

General Obligations 13-107 applied, and the claims, rights and remedies transfer with the certificate.

U.S. Bank cites to other opinions, the one opinion from Magistrate Netburn most recently that was submitted as recent authority. That case differs significantly from this case. And the key distinguishing factor is that class was attempting to certify not only current holders but prior holders. And if you look at General Obligations Law 13-107, the transferred automatically, and it would require the Court to look into: Do those prior holders have claims? What's the residency of those prior holders? What state law would apply to those prior holders claims? Those issues that were highlighted and identified and caused concern to Magistrate Netburn not exist in this case. General Obligations Law 13-107 clearly applies. It's consistent with the authority from courts in this district finding that it does apply.

And the Court need only look at U.S. Bank's own arguments. They're arguing before your Honor that 13-107 doesn't apply in this case. Separately, they have argued in front of other judges in the Oklahoma case that it did apply, and they used that as a shield to prevent them from having liability to prior holders. They argued it was simple, it was unequivocal that New York law applied and unequivocal that 13-107 applied, and they successfully dismissed the claims brought by prior holders. They now take the exact opposite

position in this litigation arguing that in doesn't apply, because now it's only current certificate holders who are bringing these claims. They can't make one argument in the courtroom next door and a different argument in this courtroom. New York law applies, the notes are clear, 13-107 is a transfer of the claims, and that's common to all members of the class.

The other argument they raised on individualized issues is a speculative statute of limitations defense. And courts are clear that in order to consider a statute of limitations defense and whether or not it creates individualized issues, that claim and defense must be meritorious. U.S. Bank has taken no steps to establish its defense. It hasn't even identified when it alleges that the class members' claims accrued. The only evidence that they provide is speculation and one example of a potential investor in Delaware who may have known and if they found out. That's not evidence establishing a meritorious statute of limitations defense.

We meet each of the elements of Rule 23(a), numerosity, commonality, typicality, and adequacy. We addressed those in the papers, and I will stand on the papers with respect to that. We also meet the predominance and superiority of Rule 23(b)(3). And unless the Court has any additional questions for me, I have nothing further other than to reserve a few minutes on rebuttal.

THE COURT: All right. Mr. Adler, is there anything you want to add the papers?

MR. ADLER: There is, your Honor, just briefly. I will talk about why there isn't commonality or predominance here when it comes proving liability, and I will also address the standing issues that Mr. DeLange was talking about when it comes to the application of 13-107, and why in the breach of contract claim they will be overwhelmed by individual issues as we look at standing.

And then my colleague, Mr. Chaiten, would like an opportunity to briefly address some of the standing issues that arise out of the Trust Indenture Act claim as well as some of the damages issues, how we don't have any compliance with *Comcast* it also creates individualized issues, and there are a number of conflicts. And time permitting, your Honor, and if your Honor directs us otherwise, Mr. Chaiten will probably briefly address superiority.

What I want to say, your Honor, just on commonality and predominance, and this is addressed in our papers, but we have to look at the Retirement Board case to see that we require loan by loan, trust by trust proof. And when Judge Forrest applied that standard here, when plaintiffs made their argument for common nucleus of operative facts, she rejected all the arguments they made here today they made in their papers. She rejected the notion that there could be proof

across these 24 different trusts, 130,000 some-odd loans, different originators, different servicers, different types of loans, she rejected all of that, your Honor.

And your Honor, if my colleague may approach just for a moment, we prepared a deck that just has a number of slides.

THE COURT: I want to tell you, I have read the papers, they're quite voluminous, I don't really need -- I certainly don't need a PowerPoint presentation. And I have given you an opportunity to speak, but not an opportunity to repeat all the arguments you made in the briefs, because that would be a waste of time.

MR. ADLER: Fair enough, your Honor, let me address the standing issue.

With respect to the note -- and this all came up in plaintiff's reply brief, so we really didn't have an opportunity to address it. They're really betting the farm on the language of the note, and they're saying New York governing law applies to that note, therefore, it applies to every transfer. There's nothing in the note that says it applies to the transfers. And in fact, it would be quite astonishing if it did because these transactions take place all over the world. And New York has a policy against the extraterritorial application of its laws, so we have transactions between German banks and Irish banks. All of this is set forth in the expert report of John Dolan. So it can't apply in those

circumstances, and there's nothing in the language of the note that says it does apply.

The *Oklahoma Police* case, your Honor, it is correct that we, several years ago in that case, made the argument that because of the governing law provision in the governing agreements we said that the transfer was also governed by New York law. In light of developments in the law, in light of Judge Nathan's decision, we just don't think that's persuasive anymore. Ultimately, though, it is an issue of law.

And then what I would just add, your Honor, even if 13-107 does apply, if it somehow applies to all of these transactions across the world, and the plaintiffs described it as hundreds of thousands of transactions, we still have to do this detailed tracing that both Judge Netburn and Judge Nathan found incompatible with class certification.

THE COURT: Your adversary made the argument that this case is very different from the case that was before Judge Netburn and now is in front of Judge Failla for purposes of considering the report and recommendation. So what do you say?

MR. ADLER: It really isn't different, because while they have defined their class as a class of current holders, the fact is that these current holders are relying on the claims of all the prior holders. So we still need to do the tracing. We need to know who the prior holders were. We need to know the circumstances of their transactions so that we

could apply New York choice of law rules, we could apply to decide whether New York really did apply to all of these transfers. The 13-107 and the language in the note doesn't somehow get them application of New York law in all of these transfers all over the world to show they actually have standing.

THE COURT: Mr. DeLange argued just a moment ago that it's your burden to show that you have a meritorious defense with respect to the statute of limitations. What do you say about that?

MR. ADLER: Well, your Honor, we have made that demonstration, so were the Delaware statute of limitations were to apply, many of these named plaintiffs themselves, and most assuredly many of the putative class members are Delaware entities, and if the harm occurred in Delaware, that's were the prior holder, the assigner of claim resided at the time, that's where they felt the economic impact, we would be applying a three-year statute of limitations, not New York's six year under CPLR 202. We have made that showing in our papers, your Honor. There are also other transactions. The State of Alaska is a prior holder here as well, three-year statute of limitations; Province of Ontario, two-year statue of limitations.

So we have made the demonstration that this would be a meritorious defense, and we need to look then and do all of

this detailed tracing to decide which jurisdiction's law is going to apply.

THE COURT: All right. Go ahead.

MR. ADLER: I'll turn things over to Mr. Chaiten to address a couple of issues.

THE COURT: All right.

MR. CHAITEN: I will be very brief, your Honor. I wanted to address briefly three issues and how they relate to class cert. One is the issue of TIA standing, damages, and superiority.

On the question of TIA standing, the Court can read *Bluebird*, the Second Circuit's decision, and Judge Mukasey's decision in *LNC*. They're pretty clear: If you don't have out-of-pocket losses, you don't have standing for TIA purposes. And for the only named plaintiffs for 20 of these trusts invested in tranches that never had realized losses; not just one they held, but never at any point. At least in *LNC* and *Bluebird* there were bonds that had realized loss, the question was who actually suffered the loss. Here for 20 of these named plaintiffs there has never been a realized loss, so there can't be TIA standing.

And on the standing issue, I would like to address a few points that they made in the reply brief. We obviously didn't get a surreply, so those are new issues. They tried to define the injury as an injury to the trust; say we have

increased investment risk, and therefore the out-of-pocket loss requirement shouldn't apply. But injuries to the trust that don't affect the individual provide no basis for TIA standing for an individual. It has to have an impact in realized losses, out-of-pocket losses for the individual. They tried to distinguish *Bluebird* in terms of timing. They say here the breaches occurred after we brought, which is not true, and we documented that in the expert reports.

But in any event, the timing doesn't matter if you invested in a tranche that has had zero realized losses. They say well, how can you require out-of-pocket losses of us when we're current holders? But current holders can have out-of-pocket losses; they're realized losses, they're missed principal and interest payments, or they could sell at a loss if they could sell at a loss, but these people would profit if they sold.

And finally, they say the Second Circuit hasn't imposed an out-of-pocket loss requirement for other securities laws. And I don't really have anything to add to Judge Mukasey's discussion of that in *LNC*. He says that's just not true with a TIA. He explains why. There's prudent person obligations speculating about what would have happened and when is inappropriate until -- you really have to cap things, you can't allow recovery for people who haven't had out-of-pocket losses. And as for the other four trusts where the named

plaintiff is invested in a tranche that had out-of-pocket losses, there still is going to be individualized issues determining who within the class has out-of-pocket losses and standing to bring a TIA claim.

And then on damages I just wanted to make one quick point. Their damages model is, as explained in the brief, a trust level model. It determines what they call trust level damages and just gives them all to current holders. And that is going to lead to -- first of all, there's a mismatch between that and their theories of liability. It's not a model for a TIA, it can't be, and they're not going to argue that's a model for the TIA, so there's a mismatch with half of the case there.

And then if you just look at some examples, they propose they're going to figure trust level damages, figure out how much is the waterfall as of today, rather than when the money would have gone through the trust to figure out which tranches get the money, and then give every noteholder in the same tranche the same amount of money regardless of when they purchased, regardless of whether they lost or gained.

So, for example, the only named plaintiff for one of the trusts in the case, BAYRT 2005-E, PIMCO Income Fund, bought in 2012, seven years after issuance, years after the market upheaval in this case, at $46. IDC prices, vendor pricing for that note is $86 today. They want to give that plaintiff, that named plaintiff, the same amount per note as a class member who

bought -- an absent class member who bought at issuance at par and has lost money. That is not an individualized damages model, and it leads to profound conflicts, because what do you think at that absent class member will say about that model? He will say no, the person who profited shouldn't recover, I should recover, I should get the money. It's a pretty profound conflict.

And how do we know this conflict is real? Their own expert -- and this is discussed in our expert's report, Dr. James' report -- their expert, Dr. Hatzmark, filed an expert report in another RMBS trust fee case, Chicago Police, it was against U.S. Bank, TIA claims and contract claims. And in that case he came up with a model that said when we're figuring out within a trust within a tranche who is going to recover and who is not, he said those investors with overall gains in their investment, by reference to their current holding position, are not eligible for recovery as to that certificate. Now today he's representing -- he's retained by people who have actually gained money, and what is he saying? Well, we'll actually divide it up. Even though we gained, we'll divide up the money. So it doesn't matter which is right, if any of those approaches are right, the point is that people are going to want to represent their own interests and not have these plaintiffs represent their interests.

Lastly, on superiority, just a few words, I mean all

the reasons discussed in the brief and discussed today, the predominance issues, the tracing issues, the loan by loan and trust by trust, the conflicts or reasons that a class action is not superior, but another way of looking at this is what happens if you deny class cert?

Well, you avoid all those problems. You avoid all the manageability issues. As for named plaintiffs, it's not a death knell for them. They're large sophisticated investors with big investments and they can proceed individually with their claims. This isn't some consumer class action where they're seeking to recover two dollars for a container of yogurt or something; nor is there any evidence that the courts will be flooded with individual claims. And Magistrate Judge Netburn explained the reasons. These are sophisticated investors, and to the extent they agree with these plaintiffs' view of what the trustee should have done, they would have already sued.

In fact, Dr. Hatzmark, their expert, identified 272 holders in all of these trusts, and 80 of them are already named plaintiffs in this case. So there's no evidence there's a large number of individual suits beyond whatever has been filed already that is going to suddenly appear if the Court denies class cert.

So I respectfully say class certification has nothing left to commend it, and we urge the Court to deny plaintiff's

renewed motion for class certification.

THE COURT: Mr. DeLange, did you want to make some additional comments?

MR. DeLANGE: Your Honor, if could briefly respond to a few of the arguments from U.S. Bank. First, with respect to the damages model, our damages model tracks the theory of liability in this case, and comparing it to another case with a different theory of liability, of course that damage model in another case may differ because there's a different theory of liability.

The theory of liability here is that U.S. Bank has breached and is continuing to breach its duties and obligations under the contract. That includes notice of breaching loans -- of loans that breach reps and warranties, it includes ongoing servicing violations. Our damages model will calculate only those damages caused by U.S. Bank's failure to act. It will isolate those loans that breach reps and warranties that U.S. Bank discovered and took no action.

Those loans and the amount of money of the damages caused by that, yes, it will go to the trust. But as Judge Forrest recognized in the motion to dismiss opinion, and also as Judge Scheindlin recognized in her motion to dismiss opinion in the *HSBC* case, the trust is a pass-through entity. The money passes through to the certificate holders. That's how it was set up and how it was intended. That's how the damage

model will calculate total damages and allocate those damages to the individual current certificate holders. This is the certificate holder's damage. It is their claim. They're bringing those claims. The damage model is consistent with *Comcast* and follows plaintiff's theory of liability in this action.

I want to briefly address the tracing. They argue that somehow we still have to trace even if General Obligations Law 13-107 applies, which we believe it does, they still claim that they're going to have to trace all of these transactions.

There's a problem. Discovery is over in this case. They had an opportunity to conduct all that discovery. We provided them with our prior holder information who we obtained the certificates from. They had the opportunity to trace it all the way back to the beginning if they so choose. They didn't do that. And we're beyond discovery. We're not at a stage where tracing it all the way back is going to become the focus of this litigation or a focus of discovery.

I want to address briefly superiority since they touched on it. The only case they cite is the *Board of Trustees of Southern California* finding that a class action was not superior and that the individual sophisticated investors could bring their own claims. The problem in that case is there were nine potential class members, that's it, only nine. Here you have 272, and as Dr. Hatzmark opines, likely

significantly more than 272.

Finally, with respect to TS standing, they rely heavily on the *LNC* decision. As the Court is aware, TIA does not define damages as out-of-pocket losses, it is defined as actual damages. The judge in *LNC* acknowledged that while he was using out-of-pocket losses in that particular instance, there could be other measures of damages. And importantly, for standing purposes, recognized that an investor can purchase into a trust knowing that the trustee has breached its duties and still have damages if the trustee continues to breach its duties after the purchase. And we definitely have that here.

With respect to the example of PIMCO purchasing in 2012, U.S. Bank had the ability in 2012 and after that purchase to cure the servicing violations, to provide notice of the breaches of reps and warranties. They didn't do so. They breached their duties and are continuing to breach their duties, and all the plaintiffs have standing under to TIA to assert their claims.

Unless the Court has any additional questions, I have nothing further.

THE COURT: All right. Mr. Adler, Mr. Chaiten, what do you say to Mr. DeLange's point that discovery is over and nobody paid any attention to finding the tracing during discovery and so this sort of a red herring issue? What do you say?

MR. ADLER: Your Honor, first, we're talking about standing issues, so it's plaintiff's burden to demonstrate standing for themselves and the putative class. They haven't done so with all of these issues. We didn't embark on this detailed tracing obligation that they're trying to somehow now put back on to us.

And the other aspect here, your Honor, is were this somehow to fall on us, we still haven't had absent class member discovery in this case. If a class is certified we're certainly going to be asking for that discovery to deal with some of our defense issues as well. But bottom line, your Honor, it's their obligation to demonstrate standing, not the reverse.

THE COURT: Let me start with some factual background.

Plaintiffs are investors and noteholders in 25 Delaware statutory trusts created between 2004 and 2007 that issued residential mortgage-backed securities. These securities were secured by loans valued at nearly $19.8 billion at the time of securitization. (Citing Am. Cmplt. (Dkt. No. 74) 1, 19, 27; as well as the DeLange Decl., Ex. 1 (Dkt. No. 221-1) 14-15, and Appendix C at 46) The current principal balance of these Trusts is $3.35 billion, and the Trusts have suffered total realized collateral losses of nearly $2 billion. (Id. 27, Ex. 3; DeLange Decl., Ex. 1 (Dkt. No. 221-1), and Appendix C at 46). Defendant U.S. Bank acts as Indenture Trustee, and

is responsible for administering the Trusts in the interests of the Noteholders. (Id. 1, 34-35)

The Trusts were created to facilitate the securitization and sale of residential mortgage loans to investors, and the Trusts' assets consist entirely of the underlying loans. (Id 2)

The securitization process is as follows: An "Originator" - usually, a financial institution - makes mortgage loans to borrowers. (Id. 3, 10, 36; Chaiten Decl., Ex. B (Dkt. No. 225-2) paragraph 14) An entity known as a "Sponsor" then creates a loan pool from mortgages it originated directly or purchased indirectly from other originators. (Id. 36) Once the loans are selected for securitization, the Sponsor - through an affiliate known as a "Depositor" - transfers the loan pools to the Trusts. (Id 3, 37; Chaiten Decl., Ex. B (Dkt. No. 225-2) paragraph 14) The Depositor segments the cash flows and loans in the loan pool into different tranches, which reflect varying levels of risk. (Id. 37; Chaiten Decl., Ex. B (Dkt. No. 225-2) paragraphs 14-15)

The Trusts then issue notes to investors that represent the obligations of the Trusts. (Id. 2, 31) The notes are collateralized entirely by the underlying mortgage loans held in the Trusts' mortgage pools, and cash flows from the loan pool - derived from principal and interest payments of mortgage borrowers - are paid to investors. (Id. 2, 31) Cash

flows from the mortgage loans are allocated to investors in the different tranches according to prioritization rules - commonly referred to as waterfall provisions - contained in each securitization's governing agreements. (Id. 37; Chaiten Decl., Ex. B (Dkt. No. 225-2) paragraphs 14-15) Cash flows are generally applied in order of priority, with returns going to the most senior tranches first. By contrast, losses to the loan pool due to defaults, delinquencies, or foreclosure are applied in reverse order of seniority, affecting the most junior tranches first. (Id.)

The Noteholders' rights and U.S. Bank's contractual duties - as Indenture Trustee - are set forth in certain securitization agreements, including the Mortgage Loan Purchase and Sale Agreements, the Trust Agreement, the Sale and Servicing Agreement, and the Indenture Agreements. I will refer to these agreements collectively as the "Governing Agreements". (Id. 42)

The Mortgage Loan Purchase and Sale Agreements are contracts between either the Originator and the Sponsor, or the Sponsor and the Depositor, and they govern the terms of the sale of the mortgage loans acquired for securitization. (Id. 44) In its capacity as a "Seller" under the Purchase and Sale Agreements, the Originator or Sponsor agrees to certain representations and warranties contained in these agreements regarding the credit quality and risk profile of the mortgage

loans held by the Trust. (Id. 44-45) Moreover, upon discovery or receipt of notice of any breach of the Seller's representations and warranties that has a material adverse effect on the value of the loan pools in the Trusts, the Seller is required to cure, substitute, or repurchase the defective loans. (Id. 46-47)

The Trust Agreement is the operative document that creates the Delaware statutory trust. (Id. 51) It is a contract between the Depositor - also referred as the "Owner Trustee" - and other entities. (Id.) The Trusts acts as the "Issuer," issuing notes to various investors. (Id.)

The Sale and Servicing Agreements are contracts between the Depositor, the "Servicers," the Issuer, the Sponsor and U.S. Bank in its capacity as Indenture Trustee. (Id. 52) Under these agreements, the Depositor conveys its right, title, and interest in the mortgage loans to the Issuer - that is, the Trust - and the Issuer conveys notes to the Depositor, which are then resold to underwriters, who in turn sell the notes to investors. (Id. 38-39, 52) The Sale and Servicing Agreements also impose obligations on the "Master Servicers" to supervise, monitor, and oversee the obligation of the servicer to service the loans. (Id.)

Finally, the Indenture is a contract between the Trusts - the Issuers - and U.S. Bank as Indenture Trustee, under which the Issuers issue notes. (Id. 53) Under the

Indenture, the Issuer pledges its rights in the notes to the Indenture Trustee, which is responsible for securing the payment obligations on the notes on behalf of the beneficial owners. (Id.)

Accordingly, the Governing Agreements establish certain rights and duties of U.S. Bank as Trustee, to be exercised for the benefit of the Noteholders. (Id. 50, 54) With respect to the Sellers/Sponsors, U.S. Bank's responsibilities include a duty "to give prompt written notice to all parties upon its discovery of a breach of a [representation and warranty] made by a seller," and to enforce the obligations of the seller to cure, substitute, or repurchase the defective loans. (Id. 46-47, 56)

Under the Sale and Servicing Agreements, U.S. Bank also has obligations upon occurrence of a Servicer "Event of Default," which is defined as a specified failure of the servicer to perform its servicing duties and cure this failure within a specified period of time. (Id. 58) If a Servicer Event of Default occurs, and U.S. Bank as indenture trustee has received written notice of or has actual knowledge of this default, U.S. Bank is required to give prompt, written notice to the Servicer and all noteholders. (Id. 57, 59) The remedies for uncured Servicer Events of Default include termination of the Servicer and recoupment of Trust assets lost as a result of the Servicer's violations. (Id. 60)

The Indentures similarly impose obligations on U.S. Bank, as Indenture Trustee, in the event that it learns of an Event of Default. (Id. 63) If U.S. Bank becomes aware of or receives written notice of an Event of Default, it must use the same degree of care and skill in responding to the default as a prudent person would under the circumstances. (Id. 59, 64) The Indenture Trustee must also provide notice to the Noteholders of any Event of Default of which it becomes aware. (Id. 65)

Plaintiffs here assert that each of the "Trusts loan pools contains a high percentage of loans that materially breached the seller's representations and warranties," adversely affecting the value of those loans and the Trusts' and Noteholders' rights in those loans. (Id 66) In particular, plaintiffs assert that various representations and warranties were "systematically and pervasively false," including the originator's compliance with underwriting standards, owner-occupancy statistics, appraisal procedures, and loan-to-value ratio. (Id.) Plaintiffs point to the following as evidence of such breaches: The high default rate of the mortgage loans; collateral losses suffered by the Trusts; plummeting credit ratings of residential mortgage backed securities generally; sellers' routine abandonment of underwriting guidelines; fabrication of borrower loan information; predatory and abusive lending; and the results of

forensic reviews and re-underwriting of loans within the Trusts in other litigation. (Id.)

The Amended Complaint goes on to allege that as a result of delinquencies, loan modifications, borrower defaults, and foreclosures, the Trusts incurred large collateral losses. (Id. 69) By January 1, 2009, collateral losses amounted to more than $500 million, and an average of one in every five loans in the Trusts was delinquent. (Id. 7, 69) Nine Trusts had delinquency rates exceeding 20%, and three Trusts had delinquency rates of more than 40%. (Id. 7) By January 1, 2011, realized collateral losses amounted to $1 billion. (Id.) And by the start of 2010, nearly all of the securities issued by the Trusts had been reduced to "junk" status. (Id.)

Plaintiffs allege that "beginning in 2009 and by 2011," U.S. Bank was aware that each of the Trusts' loan pools contained high percentages of mortgage loans that materially breached the representations and warranties. (Id. 89) Despite this knowledge, U.S. Bank failed to comply with its obligations under the Governing Agreements to protect the Trusts and Noteholders. (Id. 141) According to Plaintiffs, U.S. Bank's alleged breaches have harmed the Trusts by depriving the Trusts of valuable remedies that would have prevented the Trusts from incurring substantial losses. (Id. 161, 172) Plaintiffs also claim that the Noteholders suffered injury because U.S. Bank's breaches "diminished the value of the notes held by the

Noteholders" and "prevented the Noteholders from protecting the rights of the Trusts." (Id. 173)

As a result of Judge Forrest's rulings on a motion to dismiss, only the First and Second Causes of Action of the Amended Complaint remain. The First Cause of Action is a breach of contract claim in which Plaintiffs allege that U.S. Bank violated its obligations under the Governing Agreements. (Id. 163-173). According to Plaintiffs, U.S. Bank had knowledge and notice of triggering Events of Default and did not give proper notice of the default to, among others, the noteholders. Plaintiffs also claim that U.S. Bank did not take appropriate steps to enforce the rights of the Trusts with respect to the breach. (Id. 166, 170-171)

In the Second Cause of Action, Plaintiffs allege that U.S. Bank breached its duties and responsibilities under the Trust Indenture Act by failing to provide notice of defaults, and by failing to act prudently to enforce the Indenture Trustee's rights to, among other things, enforce the seller's obligations to repurchase, substitute, or cure defective mortgage loans, and to require the servicers to cure all servicing breaches and reimburse the Trusts for losses caused by servicing violations. (Id. 175-176)

Pending before the Court is Plaintiffs' motion for class certification. (Dkt. Nos. 218-227) Plaintiffs have moved to (1) certify "a class of all individuals who purchased

or otherwise acquired a beneficial interest in a security issued from the Trusts . . . between the date of offering and 60 days from the final order certifying the class and who hold that beneficial interest in the security through the date of final judgment in the District Court, and who were damaged as a result of Defendant U.S. Bank['s] . . . alleged breaches of contract and violations of the [Trust Indenture Act]"; (2) appoint Plaintiffs as Class Representatives for the respective Trusts in which they hold notes; and (3) appoint Bernstein Litowitz Berger & Grossman LLP as Class counsel. (Pltf. Br. (Dkt. No. 219) at 7)

Defendant opposes the class certification motion, noting that this case involves "holders in 25 different trusts comprising 227 unique securities trusts backed by 46 separate loan groups and more than 100,000 loans originated by 19 different originators and 23 different servicers." (Def. Br. (Dkt. No. 224) at 8)

In opposing class certification, Defendants contend that: (1) because there is no "common nucleus across the trusts," Plaintiffs' claims require loan-by-loan and trust-by-trust proof and, as a consequence, individualized questions predominate and the class lacks commonality; (2) Plaintiffs' lack of actual injury under the Trust Indenture Act deprives this Court of subject matter jurisdiction over 21 of the Trusts; (3) Plaintiffs' rely on prior noteholders' claims

and injuries, necessitating individualized hearings and tracing of note ownership that independently precludes class certification; (4) Plaintiffs' damages model provides no basis for class certification; (5) intra-class conflicts preclude certification because the proposed class representatives are inadequate representatives with interests antagonistic to the class; and (6) Plaintiffs have failed to meet their burden of establishing ascertainability, numerosity, and superiority. (Def. Br. (Dkt. No. 224))

I conclude that the motion for class certification should be denied because Plaintiffs are required to demonstrate out-of-pocket losses for purposes of their Trust Indenture Act claim, and have not done so with respect to notes issued by 21 of the Trusts. Plaintiffs thus lack standing to pursue these claims, and this Court lacks subject matter jurisdiction to hear them. The damages model proffered by Plaintiffs also provides no basis for granting class certification here.

I will begin with the standing issue. In opposing the motion for class certification, Defendant argues that Plaintiffs have not demonstrated actual injury. (Def. Br. (Dkt. No. 224) at 18-27) Defendants note that it is undisputed that each named Plaintiff is a current Noteholder in the Trusts, and that many of the named Plaintiffs bought their notes recently - long after the 2008 financial crisis - and have profited from their investments. (Id. at 11, 18; see also

Pltf. Reply (Dkt. No. 219) at 12 ("Plaintiffs' liability theory extends only to current Noteholders, for whom out-of-pocket losses are inapplicable.")

Plaintiffs contend, however, that as current Noteholders, they have standing to assert the claims of prior holders under New York General Obligations Law § 13-107's rule of automatic assignment. (Pltf. Reply (Dkt. No. 222) at 8; Pltf. Ltr. (Dkt. No. 132) at 1-2)

Defendant responds that the General Obligation Law does not apply to the Trust Indenture Act, that the Trust Indenture Act requires "actual damages," and that Plaintiffs lack standing under the Trust Indenture Act. In this regard, Defendant notes that Plaintiffs have suffered no out-of-pocket losses related to their holdings in 21 of the Trusts. (Def. Br. (Dkt. No. 224) at 24-25) Defendant further contends that Plaintiffs' alleged lack of standing under the Trust Indenture Act and Article III deprives this Court of subject matter jurisdiction over claims relating to 21 trusts, and requests that this Court decline to exercise supplemental jurisdiction over the state law breach of contract claims relating to these trusts. (Id. at 24-26)

Standing is, of course, a "'threshold question in every federal case, determining the power of the court to entertain the suit[;]'" it derives from Article III's case-or-controversy requirement. *Denney v. Deutsche Bank AG*,

443 F.3d 253, 263 (2d Cir. 2006). "The filing of suit as a class action does not relax this jurisdictional requirement." (Id.) Accordingly, "[i]f plaintiffs lack Article III standing, a court has no subject matter jurisdiction to hear their claim." *Cent. States Se. & Sw. Areas Health & Welfare Fund v. Merck-Medco Managed Care, L.L.C.*, 433 F.3d 181, 198 (2d Cir. 2005).

"In a class action, '[t]he initial inquiry is whether the lead plaintiff individually has [Article III] standing.'" *Indergit v. Rite Aid Corp.*, No. 08 CIV. 9361 (PGG), 2009 WL 1269250, at *3 (S.D.N.Y. May 4, 2009). In order to demonstrate individual standing, "every federal plaintiff [must] establish, for each claim he seeks to press, a [(1)] personal injury [(2)] that is fairly traceable to the defendant's conduct and [(3)] likely to be redressed by the requested relief[.]" *Ret. Bd. of the Policemen's Annuity & Ben. Fund of the City of Chicago v. Bank of New York Mellon*, 775 F.3d 154, 159 (2d Cir. 2014). "'The burden to establish standing rests on the party asserting its existence.'" *In re AOL Time Warner, Inc. Sec. & ERISA Litig.*, 381 F. Supp. 2d 192, 245 (S.D.N.Y. 2004).

In order to establish injury-in-fact for purposes of Article III standing, "'a party must allege "a distinct and palpable injury to himself', and 'cannot rest his claim to relief on the legal rights or interests of third parties[.]'" *Bluebird Partners, L.P. v. First Fid. Bank, N.A. New Jersey*, 85

F.3d 970, 973 (2d Cir. 1996). However, it is also well-established that a valid "assignment of claims transfers legal title or ownership of those claims and thus fulfills the constitutional requirement of an 'injury-in-fact.'" *W.R. Huff Asset Mgmt. Co., LLC v. Deloitte & Touche LLP*, 549 F.3d 100, 108 (2d Cir. 2008).

Separate and apart from Article III's standing requirements for the named plaintiffs to sue in their own right, the named plaintiffs must also have "class standing" to sue on behalf of absent class members. *NECA-IBEW Health & Welfare Fund v. Goldman Sachs & Co.*, 693 F.3d 145, 158 (2d Cir. 2012). In *NECA*, the Second Circuit explained that even though the plaintiff "ha[d] Article III standing . . . in its own right" as to certain certificates it had purchased, the plaintiff "clearly lack[ed] [individual] standing to assert such claims" related to "[c]ertificates from other [o]fferings, or from different tranches . . . because it did not purchase those [c]ertificates." (Id.) Accordingly, the question of a named plaintiff's "'class standing' to bring claims related to . . . certificates that it had not purchased on behalf of the absent class members who had purchased them" requires a separate inquiry. *Retirement Board*, 775 F.3d, 160.

The Second Circuit has "distilled a two-part test for class standing . . . derive[d] from constitutional standing principles[:]"

[I]n a putative class action, a plaintiff has class standing if he plausibly alleges (1) that he personally has suffered some actual injury as a result of the putatively illegal conduct of the defendant, and (2) that such conduct implicates the same set of concerns as the conduct alleged to have caused injury to other members of the putative class by the same defendants.

Id. at 161 (quoting *NECA*, 693 F.3d at 162). The first prong of the "class standing" test is duplicative of the requirement that the named Plaintiffs have individual standing. *See NECA*, 693 F. 3d at 158, 162.

With respect to the second prong, the named Plaintiffs need not demonstrate identical injuries as those to whom they are seeking to represent. *See NECA*, 693 F.3d at 162 (holding that the district court erred in requiring *NECA* to demonstrate that its injuries were "the same" as those allegedly suffered by purchasers of other certificates). However, plaintiffs must establish that "the named plaintiff[s'] claims implicated the 'same set of concerns' as absent class members' claims[,]" such that one could "conclude that the named plaintiff had the right incentives." *Retirement Board*, 775 F.3d at 161. In making this determination, courts must consider whether "the proof contemplated for all of the claims would be sufficiently similar." (Id.) (Holding that the named plaintiffs lacked "class standing" on behalf of the trusts in which they had not

invested because the trustee's "misconduct must be proved loan-by-loan and trust-by-trust"); see also *NECA*, 663 F.3d at 164 (holding that the certificates' tranches and "varying levels of payment priority [did not] raise such a 'fundamentally different set of concerns' as to defeat class standing because "all of the Certificate-holders' cash flows within any such Offering . . . derive from loans originated by some of the same originators[,]" and "each Certificate-holder within an Offering . . . backed by loans originated by similar lenders has the same 'necessary stake in litigating' whether those lenders . . . abandoned their underwriting guidelines").

Once the named plaintiffs establish the requisite standing, "there is no requirement that [each] member of the class also proffer such evidence." *Denney*, 443 F.3d, 264. "At the same time, no class may be certified that contains members lacking Article III standing." (Id.) Accordingly, "[t]he class must . . . be defined in such a way that anyone within it would have standing." (Id.)

Finally, there is the requirement of so-called "statutory standing." Although sometimes referred to as an aspect of "prudential standing," the "Supreme Court has since clarified that 'statutory standing' involves the scope of the cause of action authorized by Congress and is not an element of standing under Article III." *Retirement Board*, 775 F.3d at 160 n. 5 (citing *Lexmark Int'l, Inc. v. Static Control Components,*

Inc., 134 S. Ct. 1377, 1388 n. 4 (2014)). Statutory standing asks "[w]hether a plaintiff comes within the zone of interests [protected by the statute] . . . using traditional tools of statutory interpretation" that is, "whether this particular class of persons ha[s] a right to sue under this substantive statute." *Lexmark*, 134 S. Ct. at 1387-88.

I will now discuss Article III and statutory standing as it applies to Plaintiffs' Trust Indenture Act Claims, beginning with what I believe to be the applicable law.

As noted above, in order to demonstrate individual Article III standing, "every federal plaintiff [must] establish, for each claim he seeks to press," injury-in-fact. *Retirement Board*, 775 F.3d at 159. Although a valid assignment can satisfy injury-in-fact for purposes of Article III standing *(see W.R. Huff*, 549 F.3d at 108), the *Bluebird* case demonstrates that New York General Obligations Law § 13-107 does not apply to claims arising under the Trust Indenture Act. *See Bluebird*, 85 F.3d at 973 (finding Section 13-107 inapplicable because "federal law governs the assignability of claims under the federal securities laws"). Under federal law, "federal securities law claims are not automatically assigned to a subsequent purchaser upon the sale of the underlying security." (Id. at 974.)

Accordingly, in order to satisfy individual Article III standing requirements for their Trust Indenture Act claim,

Plaintiffs must establish a traditional injury-in-fact. "An injury-in-fact must be 'distinct and palpable,' as opposed to 'abstract,' and the harm must be 'actual or imminent,' not 'conjectural or hypothetical.'" *Denney*, 443 F.3d at 264. In cases involving Trust Indenture Act claims similar to those raised here, courts have found injury-in-fact where the plaintiffs alleged that the Indenture Trustee's breaches deprived them of payments of principal and interest due on notes, or diminished the value of the notes while the plaintiffs held them, causing the notes to be sold at a loss. *See Retirement Board*, 914 F. Supp. 2d 422, 427 (S.D.N.Y. 2012) ("Plaintiffs contend that [the Indenture Trustee's] alleged conduct caused the value of their notes to drop, and they claim to have sold [the] notes . . . at a significant loss. . . . [These] damages allegations are sufficient to confer standing[.]"), aff'd in rel. part, 775 F.3d at 161 ("In this case, there is no dispute that Plaintiffs have . . . adequately pled that they have personally suffered an actual injury as a result of [the Indenture Trustee's] putatively illegal conduct."); *also, Policemen's Annuity & Benefit Fund of City of Chicago v. Bank of Am.*, 907 F. Supp. 2d 536, 546 (S.D.N.Y. 2012) ("Plaintiff asserts that the decline in the value of its certificates means that it sold the certificates at a loss and thereby suffered damages. . . . [T]hat alleged damage [is] sufficient to meet the injury-in-fact requirement[.]").

To demonstrate "statutory standing," that is, that the named Plaintiffs are entitled to bring a cause of action under the Trust Indenture Act, Plaintiffs must establish that they fall "within the zone of interests protected by the [statute]." *See Lexmark*, 134 S. Ct. at 1387-88, 1393. "The securities laws were enacted to protect those who have been injured, not treasure hunters shrewd or lucky enough to have put [their] hands on a security that once belonged to a person who was defrauded.'" *Bluebird Partners, L.P.*, 896 F. Supp. 152, 157.

Consequently, "to have standing to assert a claim for breach of the Trust Indenture Act, plaintiffs must show "that they relied on the trustees to exercise their powers and duties under the indenture as a prudent person would, that the trustees breached the prudent person standard and that plaintiffs were injured thereby." *LNC Investments, Inc. v. First Fid. Bank*, No. 92 CIV. 7584 MBM, 1997 WL 528283, at *12-13 (S.D.N.Y. Aug. 27, 1997). "[T]he trustee [must also] owe a duty [to the plaintiff] at the time of the alleged breach." Id. at 13. Furthermore, while the Trust Indenture Act's requirement of actual damages does not "bear on the type of damages that must be alleged in the Complaint[,]" it is well established that Plaintiffs must still demonstrate "a cognizable injury under the [Act]" and Plaintiffs' "eventual recovery [is limited] to their actual damages." *See Royal Park Investments SA/NV v. HSBC Bank USA, Nat. Ass'n*, 109 F. Supp. 3d

587, 612 (S.D.N.Y. 2015); 15 U.S.C. § 77www(b) ("[N]o person permitted to maintain a suit for damages under the provisions of this subchapter shall recover, through satisfaction of judgment in one or more actions, a total amount in excess of his actual damages on account of the act complained of.").

Accordingly, in *Bluebird*, the Second Circuit found that plaintiffs who purchase notes "at a discount" after the alleged breaches and injury occur lack "standing" under the Trust Indenture Act. *Bluebird*, 85 F.3d at 972-73, 975; *see also LNC Investments*, 1997 WL 528283, at *10 ("[P]laintiffs have no standing to assert [Trust Indenture Act] claims arising from misconduct that occurred and injury that was sustained before they purchased their certificates."). Where plaintiffs "purchase [their] certificates after all the alleged breaches transpired. . . and after the adverse consequences to certificate holders became painfully apparent[,] [m]arket forces assured that the price plaintiff paid for certificates which would never be wholly redeemed reflected their diminished value." *Bluebird*, 896 F. Supp. at 157. "The injury was sustained by the sellers who parted with these certificates at a reduced price, not by plaintiff[s] who purchased them at [a discount rate]," and plaintiffs lacked standing under the Trust Indenture Act. (Id.)

Likewise, where plaintiffs have purchased notes at a discount and profited on that investment, they do not fall

within the zone of interests protected by the Trust Indenture Act. See *LNC Investments*, 1997 WL 528283, at *13 (noting that plaintiff "made a profit on its investment in . . . certificates and cannot argue that as to those certificates it was injured[.]"); *see also, In re AOL Time Warner, Inc. Sec. & ERISA Litig.*, 381 F. Supp. 2d 192, 246 (S.D.N.Y. 2004) (finding that plaintiffs lacked both Article III and statutory standing under Section 11(e) of the Securities Act where the bonds purchased by the lead plaintiff increased in value, and were trading at a higher rate than when they were purchased.)

Under certain circumstances, however, plaintiffs may have standing under the Trust Indenture Act to recover on a "continuing breach theory" "for injury sustained after they purchased their [notes]," even where they purchased their notes at a "discounted price." *LNC Investments*, 1997 WL 528283, at *10. The LNC court explained that in contrast to the injury in securities cases - which "flow[s] from a one-time [discrete] misrepresentation . . . immediately reflect[ed in the purchase price] once fact of the misrepresentation is made public" - "the injury flowing from [a Trust Indenture Act] claim . . . is not so discrete, and occurs over the course of [time] as the collateral decreases in value."

When plaintiffs purchased their certificates, the market could not have accounted for future misconduct and future injury. The market had discounted the [notes] to

reflect the risk, at that time, that the [note] holders would not receive full recovery, but could not have predicted that later trustee action would increase that risk. Accordingly, to the extent that plaintiffs purchased [the notes] during the period before . . . the alleged misconduct generated increasing injury and the market was not yet fully informed of the consequences of [that risk], they have standing. (Id. at 11)

Thus, to the extent trustee misconduct "and the claimed injury - the [further] decline in the collateral's value - both occurred after plaintiffs bought their certificates, plaintiffs have standing under *Bluebird*." (Id. at 10) In contrast, "[a]ny [note] holders who purchased after [the trustee misconduct was disclosed] lack standing under Bluebird because the market insured that the price they paid reflected the diminished value of the certificates." (Id. at 12)

Even where a plaintiff proceeds under continuing breach theory of standing, however, it is well-established that "benefit of the bargain" damages do not constitute "actual damages" under the Trust Indenture Act, and that "plaintiffs' damages are limited to out-of-pocket losses." (Id. at *37-38) The LNC court reasoned as follows:

Here, all of plaintiffs' certificates were purchased at a discount, and all of the certificates sold after January 18, 1991, when the effect of the trustees' misconduct was

disclosed to the market, were sold at even greater discount. Plaintiffs purchased only that probability of full payment which was reflected in the purchase price. The market price at the time of purchase reflected the risk that the certificates would not be fully redeemed, and plaintiffs cannot argue that they expected full redemption. If the trustees' conduct resulted in a further decrease in the probability of full redemption, plaintiffs' damages are limited to that decrease that resulted from the trustees' breach, which would be reflected in the further decline of the [notes]' market price or would be apparent at maturity. Plaintiffs are not entitled to full payment on the certificates.

If, in the event of a breach of the prudent person standard the trustee became liable for the full principal amount of a certificate, regardless of the discounted purchase price for the certificate, the trustee would become the guarantor of the debt underlying the certificate. An indenture trustee does not, however, guarantee the underlying debt. . . . Effectively, when the debt issuer defaults under the indenture, the trustee promises to do what it can - exercise its rights prudently - to protect the certificate holders. If the trustee breaches that duty, which breach causes the certificates to decline in value or reduces the amount of principal recoverable, the [certificate] holders can recover what they lost: The difference between what they paid and what they

received. The indenture does not represent a bargain with the trustees or a promise that the trustees will ensure a full recovery on the certificates. . . There is no bargain on which to base benefit-of-the-bargain damages. Plaintiffs' claims rest on a tort theory of recovery, which mandates an out-of-pocket measure of damages, rather than on a contract theory of recovery. (Id. at *35, 37)

Accordingly, where, as here, a lawsuit has moved past the motion to dismiss stage, plaintiffs must demonstrate a "cognizable injury" under the Trust Indenture Act and any proposed damages model must reflect the Trust Indenture Act's actual damages requirement. *See* id. at *33 (dismissing the claims of certain plaintiffs on standing grounds where they had not demonstrated actual damages; granting defendants' motion for summary judgment to limit the remaining plaintiffs' damages under the Trust Indenture Act "to out-of-pocket losses attributable directly to the trustee defendants' breach of the prudent person standard.").

Here, Plaintiffs assert a "continuing breach" theory, contending that they satisfy both Article III and Trust Indenture Act standing requirements "because U.S. Bank's misconduct - its continuing failure to enforce Seller and Servicer claims - and the resulting injury - decline in the Trusts' assets and increased investment risk - both occurred after Plaintiffs bought their notes." (Pltf. Reply (Dkt. No.

222) at 11)

Article III requires a "personal injury" that is not speculative or abstract, however, *see*, *for example*, *Retirement Board*, 775 F.3d at 159; *Denney*, 443 F.3d at 264, and here the evidence demonstrates that Plaintiffs have not suffered any injury related to their holdings in the vast majority of the Trusts.

As in *LNC Investments*, 1997 WL 528283, at *3, Plaintiffs seek to recover under a "benefit of the bargain" theory, claiming that they are entitled to the entire "portion of the Trusts' (and in turn investors') losses caused by U.S. Bank's failure to perform its duties," "regardless of when the certificates were purchased[.]" (Pltf. Reply (Dkt. No. 222) at 12-13). Indeed, Plaintiffs concede that most of the current noteholders have suffered no out-of-pocket losses. Plaintiffs contend, however, that they are entitled to recover the entire amount of the damages attributable to U.S. Bank's alleged wrongdoing under a "benefit of the bargain" theory. (See Pltf. Reply (Dkt. No. 222) at 12 ("Plaintiff's liability theory extends only to current Noteholders, for whom out-of-pocket losses are inapplicable."); Am. Cmplt. (Dkt. No. 74) at 78; DeLange Decl., Ex. 1 (Hatzmark Expert report) 22 ("Plaintiffs seek to be put in the same position today that they would have been in had the Trustee fulfilled its obligation. Therefore . . . [the] damages methodology compensates Class Members for the

loss of the benefits they bargained for."))

As I discussed a moment ago, however, it is well-established that the Trust Indenture Act's "actual damages" provision limits Plaintiffs' recovery to out-of-pocket losses, and that noteholders can only "recover what they lost: The difference between what they paid and what they received." *LNC Investments*, 1997 WL 528283, at *35.

With respect to 21 of the 25 Trusts at issue here, there is no evidence of any type of cognizable injury under the Trust Indenture Act. *Cf. Retirement Board*, 914 F. Supp. 2d at 427 (drop in value of notes, and subsequent sale at a loss satisfies injury-in-fact); *Oklahoma Police Pension*, 291 F.R.D. at 56-57 (plaintiff's claim of "millions of dollars in losses" deriving from loss of payment on the principal and interest and diminution in value of the notes satisfies injury-in-fact). Plaintiffs have suffered no out-of-pocket losses related to their holdings in these 21 trusts. Indeed, Plaintiffs' notes in 18 of these Trusts have increased in value since Plaintiffs purchased them. (See Chaiten Decl., Ex. A (James Expert Report) (Dkt. No. 225-1) 49 n. 46, 54, Ex. 4 at 112-14 ("Exhibit 4 shows that Plaintiffs currently hold notes that are priced by Interactive Data Corp. . . above what they paid in 18 Trusts."))

Acknowledging that the *LNC* court held that a "decline in the collateral's value" could suffice for standing purposes

where the trustee's alleged wrongdoing and plaintiff's injury occurred "after plaintiffs bought their certificates," *LNC Investments*, 1997 WL 528283, at *10, the evidence here demonstrates that Plaintiffs have suffered no realized loss of principal in 21 of the trusts in which they hold notes. See Chaiten Decl., Ex. A (James Expert Report) (Dkt. No. 225-1) 49 n. 46, 53, Ex. 4 at 112). Because "Plaintiffs point to no concrete harm that actually has occurred or is imminent, and, moreover, the challenged transactions produced an economic benefit [as to eighteen of the Trusts], they have not suffered" a cognizable injury under the Trust Indenture Act. *Waxman v. Cliffs Nat. Res. Inc.*, 222 F. Supp. 3d 281, 289 (S.D.N.Y. 2016) (plaintiffs lacked Article III injury-in-fact to bring Trust Indenture Act claims where the bonds largely increased in value, and plaintiffs demonstrated no concrete harm); *LNC Investments*, 1997 WL 528283, at *10, 13 (no standing under the Trust Indenture Act where plaintiffs profited from their investment, or where plaintiffs has suffered no injury after they purchased their notes).

Because this Court's subject matter jurisdiction is predicated solely on Plaintiffs' Trust Indenture Act claim, this Court lacks subject matter jurisdiction to the extent that Plaintiffs' claims are premised on notes issued by these 21 trusts. For purposes of clarity, I will now list those 21 trusts: (1) AABST 2004-6, (2) AABST 2005-1, (3) AABST 2005-3,

(4) ACCR 2004-2, (5) ACCR 2005-3, (6) BAYRT 2005-E, (7) BAYV 2005-A, (8) GPHE 2004-2, (9) GPHE 2004-3, (10) HEMT 2006-2, (11) HMBT 2004-1, (12) HMBT 2004-2, (13) HMBT 2005-1, (14) HMBT 2005-3, (15) HMBT 2005-4 (16) HMBT 2005-5, (17) HMBT 2006-2, (18) IRWHE 2004-1, (19) IRWHE 2005-1, (20) LABS 2005-1 and (21) NYMT 2005-2. (See Chaiten Decl., Ex. A (James Expert Report) (Dkt. No. 225-1), Ex. 4 at 112-14.)

With respect to these 21 trusts for which Plaintiffs lack standing to assert claims under the Trust Indenture Act, Plaintiffs ask that this Court exercise supplemental jurisdiction over Plaintiffs' state law claim. (Pltf. Reply (Dkt. No. 222) at 12) Pursuant to 28 U.S.C. § 1367(c), however, "a district court may decline to exercise supplemental jurisdiction if it has dismissed all claims over which it has original jurisdiction." *Schaefer v. Town of Victor*, 457 F.3d 188, 210 (2d Cir. 2006). And "when all federal claims are eliminated in the early stages of litigation, the balance of factors generally favors declining to exercise pendent jurisdiction over remaining state law claims and dismissing them without prejudice." *Tops Mkts., Inc. v. Quality Mkts., Inc.*, 142 F.3d 90, 103 (2d Cir. 1998)

I see no reason to deviate from the normal rule here. Because plaintiffs' claims concerning the 21 trusts I listed above, there's no basis for subject matter jurisdiction over them, the motion for class certification will be denied.

Because Plaintiffs may choose to renew their class certification motion as to the four remaining trusts, I want to alert the parties to my concerns about two other matters. I believe that Plaintiffs' proposed damages model is improper. I will address that in a moment. First, however, I want to share my concerns about Rule 23(b)(3)'s predominance requirement as it relates to Plaintiffs' breach of contract claim and reliance on General Obligations Law § 13-107, and whether individual inquiries and note-tracing would be necessary to determine timeliness.

With respect to their breach of contract claim, Plaintiffs rely on General Obligation Law § 13-107's rule of automatic assignment to assert the claims of prior noteholders for standing purposes. (See Pltf. Reply (Dkt. No. 222) at 8) Defendant argues, however, that (1) the Trust Indenture Act precludes application of Section 13-107; and (2) even if the Trust Indenture Act did not preempt application of Section 13-107, individualized inquiries and note-tracing related to application of Section 13-107's application would preclude class certification; and (3) even if this Court ruled that Section 13-107 applies in all instances, individualized inquiries and note-tracing would still be required to determine standing and timeliness. (Def. Br. (Dkt. No. 224) at 18-24) According to Defendant, the necessity of individualized inquiries demonstrates that Rule 23(b)(3)'s predominance

requirement is not met. (Id.)

I will address only one aspect of Defendant's arguments concerning Plaintiffs' state law breach of contract claim: Whether individualized inquiries and note tracing would be required to determine timeliness.

Defendant argues that this Court would have to trace each individual note to determine whether putative class members' claims are time-barred, "because 'even if § 13-107 applies, there is 'no reliable means of collectively determining' which claims are timely." (Def. Br. (Dkt. No. 224) at 23) As to timeliness, New York's borrowing statute "requires the cause of action to be timely under the limitation periods of both New York and the jurisdiction where the cause of action accrued." *Global Fin. Corp. v. Triarc Corp.*, 715 N.E.2d 482, 484 (N.Y. 1999). For assigned claims, the cause of action accrues where the assignor's claim accrued, that is, "'where the [assignor] resides and sustains the economic impact of the loss.'" (Def. Br. (Dkt. No. 224) at 23 (quoting *Portfolio Recovery Assocs., LLC v. King*, 927 N.E.2d 1059, 1061 (N.Y. 2010)). According to Defendant, this would require this Court to (1) identify when each claim accrued; and (2) identify the holder of the note at that point. (Id.) Defendant argues that this inquiry is "far too individualized for class treatment," and that multiple states' limitations periods would apply. (Id.) Defendant further argues that the only way to

avoid this kind of individualized tracing is to limit the class to those that have held notes from the time of the earliest breach through judgment (that is, to select a class definition that requires "continuous ownership" from the date of the earliest breach). Plaintiffs' proposed class definition, however, reflects no such limitation. (Id. at 23-24) In support of its argument, Defendant cites to Judge Netburn's recent decision in *Royal Park Investments SA/NV v. Wells Fargo*, No. 14 Civ. 9764 (KPF) (SN) (S.D.N.Y. Jan. 10, 2018), at 29-30, which relied on variations in the viability of statute of limitations defenses across class members as one basis for denying class certification.

Plaintiff counters that this Court need not trace note ownership to resolve statute of limitations questions, "because the Governing Agreements and Notes mandate that New York procedural and substantive law govern." Plaintiffs also argue that U.S. Bank has not shown that variations in the statute of limitations "would pose an insuperable obstacle to class certification." (Pltf. Reply (Dkt. No. 222) at 10) Plaintiff also points out that Judge Netburn's Report and Recommendation in *Royal Park* has not yet been adopted by the District Court, and argues that Judge Netburn "overlooked a critical body of law requiring that before an affirmative defense may be considered a factor in the class action calculus, the defendant must establish that such a defense is meritorious." (Pltf.

Ltr. (Dkt. No. 250) at 3) Plaintiff further argues that "[c]ourts have been nearly unanimous . . . in holding that possible differences in the application of a statute of limitations to individual class members, including the named plaintif[f], does not preclude certification of a class action so long as the necessary commonality and, in a 23(b)(3) class action, predominance are otherwise present.'" (Pltf. Reply (Dkt. No. 222) at 11 (quoting *Steinberg v. Nationwide Mut. Ins. Co.*, 224 F.R.D. 67, 78 (E.D.N.Y 2004)).

It is true that the existence of individualized defenses across a class does not necessarily demonstrate that Rule 23(b)(3)'s predominance requirement is not met. *See, In re Nassau Cty. Strip Search Cases*, 461 F.3d at 225. ("[A]lthough 'a defense may arise and may affect different class members differently, [this occurrence] does not compel a finding that individual issues predominate over common ones.'") Rather, "[s]o 'long as a sufficient constellation of common issues binds class members together, variations in the sources and application of a defense will not automatically foreclose class certification.'" (Id.) Nevertheless, such individual issues are 'factor[s] that we must consider in deciding whether issues susceptible to generalized proof 'outweigh' individual issues,' even though 'standing alone, [they are not] sufficient to defeat class certification.'" *Johnson v. Nextel Commc'ns Inc.*, 780 F.3d 128, 138 (2d Cir. 2015). The ultimate "question

for certifying a Rule 23(b)(3) class is whether 'resolution of some of the legal or factual questions that qualify each class member's case as a genuine controversy can be achieved through generalized proof' and whether 'these particular issues are more substantial than the issues subject only to individualized proof.'" (Id.)

"[P]utative class actions involving the laws of multiple states are often not properly certified pursuant to Rule 23(b)(3) because variation in the legal issues to be addressed overwhelms the issues common to the class." *In re U.S. Foodservice Inc. Pricing Litig.*, 729 F.3d at 126-27. "[T]hese concerns are lessened[, however,] where the states' laws do not vary materially[,]" and the limited variances that exist can be effectively managed through "'certification of subclasses embracing each of the dominant legal standards[.]'" (Id. at 127) Hence, "the crucial inquiry is not whether the laws of multiple jurisdictions are implicated, but whether those laws differ in a material manner that precludes the predominance of common issues." (Id.)

"Under New York law, a claim for breach of contract must be filed within six years of when the claim accrues." *Muto v. CBS Corp.*, 668 F.3d 53, 57 (2d Cir. 2012) (citing N.Y. C.P.L.R. § 213(2)). However, "in its borrowing statute, [N.Y. C.P.L.R.] § 202, New York law also provides that 'when a nonresident plaintiff sues upon a cause of action that arose

outside of New York, the court must apply the shorter limitations period . . . of either: (1) New York; or (2) the state where the cause of action accrued.'" (Id.) And, contrary to Plaintiffs' assertions (see Pltf. Reply (Dkt. No. 222) at 10), a governing New York law provision does not preclude application of the New York borrowing statute. *See*, 2138747 *Ontario, Inc. v. Samsung C & T Corp.*, 144 A.D.3d 122, 127 (N.Y. App. Div. 2016) ("The borrowing statute is itself a part of New York's procedural law and is a statute of limitations in its own right, existing as a separate procedural rule within the rules of our domestic civil practice, addressing limitations of time . . . Thus, applying the borrowing statute is perfectly consistent with a broad choice-of-law contract clause that requires New York [law] to apply to the parties' disputes.").

Accordingly, "'[w]hen a nonresident sues on a cause of action accruing outside New York, [C.P.L.R. §] 202 requires the cause of action to be timely under the limitation periods of both New York and the jurisdiction where the cause of action accrued[.]'" *Portfolio Recovery Assocs., LLC v. King*, 14 N.Y.3d 410, 416. "If the claimed injury is an economic one, the cause of action typically accrues 'where the plaintiff resides and sustains the economic impact of the loss[.]'" *Portfolio Recovery Assocs., LLC*, 14 N.Y.3d at 416. Moreover, "when a claim has been assigned, the Section 202 analysis

focuses on the statute of limitations of the jurisdiction in which the claim accrued to the assignor." *IKB Int'l S.A. v. Bank of Am.*, No. 12 CIV. 4036 LAK, 2014 WL 1377801, at *6 (S.D.N.Y. Mar. 31, 2014).

In order to determine whether each individual claim is time-barred, this Court would have to (1) identify when each claim accrued; (2) trace the note ownership to identify who the noteholder was at the time the claim accrued and where the noteholder resided; and (3) identify and apply the limitations period of the applicable jurisdiction. To state the obvious, this would be no simple task. Institutional investors that purchased residential mortgage backed securities include entities headquartered throughout the world. (See Chaiten Decl., Ex. B (Dolan Expert Report) (Dkt. No. 225-2) 24) Indeed, Defendant has offered evidence that the institutional investors who held the notes at issue here include entities located in Germany, Luxembourg, Canada, and the United Kingdom. (Id.) Moreover, as the Dolan Report points out, there is no unique identifier for separate holdings within an RMBS tranche; instead, "each securitization is subdivided into multiple tranches identified by a CUSIP number," which applies universally to all of the interests within a given tranche. (Id. 27) Moreover, RMBS securities are typically held in "book entry" form, meaning that The Depository Trust Company's ownership records would typically only list the names of the

participant institutions, and only the participant institutions would know the name of the individual beneficial owners. (Id. 30-31)

As other courts have acknowledged, the nature of the notes at issue here, in particular the lack of "unique identifiers corresponding to individual investors' ownership interests," the geographic dispersion of broker dealers, "with ownership interests likely at times being sold off in pieces to multiple investors and individual purchase orders likely at times being filled by holdings previously acquired from multiple different sources[,]" and the absence of a "'central repository of trade history to follow changes in ownership over time,'" is such that "'reconstructing the chain of ownership of any given [note] can only be ascertained through [a] highly detailed and individualized inquiry.'" *See Deutsche Bank*, 2017 WL 1331288, at *6; *Royal Park*, No. 14 Civ. 9764, (S.D.N.Y. Jan. 10, 2018) at 30 (finding that determining the statute of limitations of the jurisdiction in which the claim accrued to the assignor would require "piecing together multiple sales and periods of ownership for just one investor, a daunting task given the lack of unique identifiers and the piecemeal trading and selling of the RMBS at issue; concluding that such an effort would require "the Court to engage in . . . individualized inquiries . . . [that] predominate over any common issues shared by the class"). It is also apparent that

the statute of limitations periods vary widely across jurisdictions. Compare Alaska Stat. § 09.10.053 (three-year statute of limitations) with N.Y. C.P.L.R. 213(2) (six-year statute of limitations period).

While Plaintiffs are correct that the question of when the alleged breaches occurred is a common question subject to "common evidence, that is, when U.S. Bank breached the contract[,]" (see Pltf. Ltr. (Dkt. No. 250) at 3), Plaintiffs do not meaningfully address the fact that determining the governing limitations period will require determining who the holder of the note was at the time of the alleged breach. And identifying prior holders requires the kind of individualized inquiries and note tracing that other courts have found incompatible with class treatment.

Moreover, Plaintiffs' argument that "U.S. Bank has failed to show how such variations would pose an insuperable obstacle to class certification" misstates the law and appears to reflect an effort to shift Plaintiffs' burden of proof onto Defendant. It is not Defendant's burden to show that variations in jurisdictions' limitations laws pose an insuperable obstacle to class certification. Instead, as I noted above, "[t]he party seeking class certification bears the burden of establishing by a preponderance of the evidence that each of Rule 23's requirements have been met." *Johnson*, 780 F.3d at 137; *see also, In re U.S. Foodservice Inc. Pricing*

Litig., 729 F.3d at 127 ("'[N]ationwide class action movants must credibly demonstrate, through an 'extensive analysis' of state law variances, 'that class certification does not present insuperable obstacles.''") Here, "plaintiffs have offered no reliable means of collectively determining how many class members' claims are time-barred." *McLaughlin v. Am. Tobacco Co.*, 522 F.3d 215, 234 (2d Cir. 2008) (finding that Rule 23(b)(3)'s predominance requirement was not satisfied because "numerous issues are not susceptible to generalized proof [and] would require a more individualized inquiry[.]").

Accordingly, this Court has grave concerns that the individualized inquiries necessary to determine whether each class member's claim is time-barred might preclude class certification.

Finally, Defendant contends that Plaintiffs' damages model "does not even purport to" measure damages under the Trust Indenture Act, and is insufficient under *Comcast Corp. v. Behrend*, 569 U.S. 27 (2013).

Defendant complains that Plaintiffs' damages model does not properly measure damages under the Trust Indenture Act because it is premised on a "benefit-of-the-bargain" methodology. (Id.) As discussed above, Defendant is correct that Plaintiffs' damages under the Trust Indenture Act are limited to out-of-pocket losses. Plaintiffs may not recover on a "benefit of the bargain" theory.

In *Comcast*, the Supreme Court stated that "a model purporting to serve as evidence of damages in [a] class action must measure only those damages attributable to [a claim's] theory [of liability]." *Comcast*, 569 U.S. 27, 35. "If the model does not even attempt to do that, it cannot possibly establish that damages are susceptible of measurement across the entire class for purposes of Rule 23(b)(3)." (Id.)

Here, Plaintiffs' damages model does not reflect the Trust Indenture Act's actual damages limitation. Indeed, in his rebuttal to Defendant's experts' reports, Plaintiffs' expert, Dr. Hatzmark, does not even attempt to measure out-of-pocket losses; instead, he defends his damages model on the grounds that "Plaintiffs' theory of liability extends only to current Noteholders," and that therefore a "benefit-of-the-bargain damages methodology" is appropriate. (DeLange Decl. II, Ex. 2 (Hatzmark Expert Rebuttal Report) (Dkt. No. 223-2) 7-8) Plaintiffs' damages model also does not account for or allocate recovery according to each investor's actual damages, that is, their out-of-pocket losses. Instead, Dr. Hatzmark's model calculates "Trust-level damages (that is, aggregate defective and servicing losses [suffered by] each Trust)". Dr. Hatzmark then distributes these damages to current noteholders in the Trust on a pro rata basis based on the number of notes held by each investor, regardless of when these noteholders purchased their notes or whether these

noteholders suffered any actual out-of-pocket losses. (*See* DeLange Decl. II, Ex. 1 (Hatzmark Supplemental Expert Rebuttal Report) (Dkt. No. 223-1) 8; Chaiten Decl., Ex. A (James Expert Report) (Dkt. No. 225-1), 51-52 ("Such a pro rata allocation does not measure individual holders' damages. Dr. Hatzmark's model assumes that the alleged economic harm is spread evenly across investors in a particular tranche regardless of when they purchased and how much they lost.")) Because Plaintiffs' damages model does not allocate damages in a manner consistent with their Trust Indenture Act claim, Plaintiffs' damages model precludes class certification. *See Comcast*, 569 U.S. at 35 ("[A]t the class-certification stage (as at trial), any model supporting a 'plaintiff's damages case must be consistent with its liability case[.]'").

Defendant also argues that Plaintiffs' damages model is not sufficient under *Comcast* because it treats U.S. Bank not as an indenture trustee, with the duties alleged in the Complaint and set forth in the governing agreements, but rather as a guarantor against all losses attributable to loans with representations and warranties breaches and servicer problems. (Def. Br. (Dkt. No. 224) at 28) Indeed, Plaintiffs' model seeks to measure damages based on a "but-for world." In this "but-for world," "but-for" the Trustee's "fail[ure] to act consistently with [its] duties . . . by enforcing the sellers' obligation to cure, repurchase or substitute mortgage loans

affected by breaches of the representations and warranties," class members "would own Notes that would have supporting collateral pools which would have held and would currently hold no defective loans." (DeLange Decl., Ex. 1 (Dkt. No. 221-1) (Hatzmark Amended Expert Report) 21-22; DeLange Decl. II, Ex. 2 (Hatzmark Expert Rebuttal Report) (Dkt. No. 223-2) 15)

"An indenture trustee does not, however, guarantee the underlying debt." *LNC Invs.*, 1997 WL 528283, at *35. Rather, "an indenture trustee merely acts for the certificate holders when their rights to recovery are threatened." (Id.) "[W]hen the debt issuer defaults under the indenture, the trustee promises to do what it can - exercise its rights prudently - to protect the certificate holders." If the trustee's breach of that duty "causes the certificates to decline in value or reduces the amount of principal recoverable, the [certificate] holders can recover what they lost[.]" Certificate holders cannot require the trustee to redeem the full value of the certificates, however, irrespective of the actual losses caused by the trustee's breaches.

Thus, an appropriate model of damages would have to account for: (1) whether and when U.S. Bank discovered the breaches; (2) whether the seller would have been in the financial position to repurchase or substitute the loan had U.S. Bank acted; (3) if not, whether litigation would have been appropriate; (4) for any litigation, whether it would have

succeeded and whether any damages would have been collectible. (*See* Chaiten Decl., Ex. A (James Expert Report) (Dkt. No. 225-1) 109-121) Plaintiffs' damages model does not address any of these issues. Accordingly, Plaintiffs' damages model fails to correspond to their theory of liability and runs afoul of *Comcast*, and thus provides another basis for denying Plaintiffs' motion for class certification.

For all these reasons, the motion for class certification is denied. I am going to ask Plaintiffs to consider this ruling, as well as my concerns about the statute of limitations issue, and send me a letter by February 16 telling me how they wish to proceed in this matter.

Is there anything further?

MR. DeLANGE: Nothing further from plaintiff. Thank you, your Honor.

MR. ADLER: Nothing further, your Honor, thank you.

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